

Internal Revenue Service

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Person To Contact:
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Date:
January 27, 2009

X =

State =

Date 1 =

Trusts =

PLR-135947-08

PLR-135947-08

PLR-135947-08

Dear _____ :

This letter responds to your letter dated August 12, 2008, requesting relief under section 1362(f) of the Internal Revenue Code.

Facts

You have represented that the facts are as follows. X is a corporation organized under the laws of State. X filed a timely Form 2553, Election of a Small Business Corporation, electing to be taxed as an S corporation, effective on Date 1. However, the income beneficiaries of the Trusts did not properly sign the Form 2553 electing to be qualified subchapter S trusts ("QSSTs"). Because the Form 2553 was not properly signed, the QSST elections of the Trusts were not valid and, therefore, X's S corporation election was not valid.

X represents that since Date 1 X and X's shareholders have filed tax returns consistent with X being an S corporation.

Law and Analysis

Section 1361(a)(1) provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 75 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation.

Section 1361(c)(2)(A)(i) provides that for purposes of § 1361(b)(1)(B), a trust may be a shareholder if all of it is treated (under subpart E of part I of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States. Section 1361(c)(2)(B)(i) provides that for purposes of § 1361(b)(1), in the case of a trust

described in section 1361(c)(2)(A)(i), the deemed owner shall be treated as the shareholder.

Section 1361(d)(1) provides that in the case of a QSST with respect to which a beneficiary makes an election under § 1361(d)(2), such trust shall be treated as a trust described in § 1361(c)(2)(A)(i) and, for purposes of § 678(a), the beneficiary of such trust shall be treated as the owner of that portion of the trust which consists of stock in an S corporation with respect to which the election under § 1361(d)(2) is made.

Section 1361(d)(2)(D) provides that an election under § 1362(d)(2) shall be effective up to 15 days and 2 months before the date of the election. Treasury Regulation 1.1361-1(j)(6)(i) provides that if the person required to elect is under a legal disability by reason of age, the election may be made by that person's guardian or other legal representative, or if there be none, by that person's natural or adoptive parent.

Section 1.1361-1(j)(6)(ii) of the Income Tax Regulations provides that the current income beneficiary of the trust must make the QSST election under § 1361(d)(2) by signing and filing with the service center with which the corporation files its income tax return the applicable form or statement including the information listed in § 1.1361-1(j)(6)(ii).

Section 1361(d)(3) provides that the term "qualified subchapter S trust" means a trust -- (A) the terms of which require that -- (i) during the life of the current income beneficiary, there shall be only 1 income beneficiary of the trust, (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary, (iii) the income interest of the current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust, and (iv) upon termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary, and (B) all of the income (within the meaning of section 643(b)) of which is distributed (or required to be distributed) currently to 1 individual who is a citizen or resident of the United States.

Section 1362(a) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1362(a)(2) provides that an election to be an S corporation will only be valid if all persons who are shareholders on the day on which such election is made consent to such election.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which it was made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, (2) the Secretary determines that the

circumstances resulting in such ineffectiveness were inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and the representations made, we conclude that X's election to be an S corporation on Date 1 was an inadvertent invalid election within the meaning of § 1362(f).

Pursuant to the provisions of section 1362(f), X will be treated as an S corporation from Date 1 and thereafter, provided that the Trusts qualify as QSSTs and provided that X's election was otherwise valid and not terminated under § 1362(d). Accordingly, the shareholders of X must include in income their pro rata share of the separately stated and nonseparately computed items of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat X as described above, this letter ruling will be null and void.

This ruling is conditioned on X, within 60 days of the date of this letter, filing a new Form 2553, Election of a Small Business Corporation, which contains the proper signatures, with the appropriate service center with an effective date of Date 1. Furthermore, the income beneficiaries of the Trusts must make QSST elections, effective Date 1, with the appropriate service center within 60 days of the date of this letter. A copy of this letter should be attached to the new form 2553 and the new QSST elections.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code, including whether X was a small business corporation under § 1361(b), or whether the Trusts are QSSTs within the meaning of § 1361(d)(3).

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,
David R. Haglund

David R. Haglund
Senior Technician Reviewer
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes

cc: